

Statement of James F. Sloan
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U.S. Department of the Treasury
before the
Subcommittee on Oversight and Investigations
Committee on Financial Services

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Madam Chairwoman, and members of the Subcommittee, thank you for this opportunity to appear before you today to discuss the Financial Crimes Enforcement Network's (FinCEN) role in combating money laundering and the fight against terrorist financing.

FinCEN's role in this effort was significantly expanded in the eighteen months following the terrorist attacks on the World Trade Center because of its mission-oriented focus on facilitating information-sharing and networking amongst the law enforcement, regulatory and financial communities and with similar units worldwide. The recent formation of the new Executive Office for Terrorist Financing and Financial Crimes (EOTF/FC) within the Department of The Treasury further underscores the value of FinCEN's support to law enforcement in identifying and tracking the financial aspects of terrorist and other criminal activity. FinCEN welcomes the establishment of this important office, which will be responsible for providing policy guidance to our bureau as we execute our responsibilities as Administrator of the Bank Secrecy Act (BSA). It will be headed by Juan Zarate, Deputy Assistant Secretary for Terrorist Financing and Financial Crimes. Mr. Zarate worked closely with our bureau in his former capacity as Deputy Assistant Secretary for Terrorism and Violent Crimes, within the Office of Enforcement, and we look forward to a continuance of that excellent working relationship.

My statement today will update the committee on FinCEN's programs, as well as the significant progress we have made in meeting our obligations under Title III of the USA Patriot Act.

Mission

FinCEN was established, in April 1990, by the Department of the Treasury (Treasury Order Number 105-08) to provide a government-wide, multi-source intelligence and analytical network. This network was designed to support the detection, investigation, and prosecution of domestic and international money laundering and other financial crimes. In May 1994, FinCEN's operation was broadened to include regulatory responsibilities and, in October 2001, the USA PATRIOT Act elevated FinCEN to bureau status.

Today, FinCEN is one of our Government's primary agencies to oversee and implement policies to prevent and detect money laundering and other financial crimes. It is a strategically focused bureau organized to network governments, people and information in support of both the law enforcement and intelligence communities. This increasingly dynamic network links the law enforcement, financial and regulatory communities domestically and internationally together for the common purpose of preventing, detecting, and prosecuting financial crime. Information sharing, analysis and networking are the key objectives in accomplishing our mission from a neutral vantage point. In fact, FinCEN's neutral posture and customer service orientation are vital elements to our success.

FinCEN works to accomplish this mission in three ways.

First, as administrator of the Bank Secrecy Act (BSA), our nation's comprehensive anti-money laundering statute, FinCEN obtains certain data from financial institutions. The law's record keeping and reporting requirements help establish a financial trail for law enforcement to follow as they track criminals, their activities, and their assets.

Second, FinCEN's intelligence analysts add value to the information collected under the BSA by uncovering leads and hidden pieces of the puzzles contained in money laundering schemes – schemes that can be highly convoluted as well as global in scope.

And finally, through technology and partnership building, these value-added products are disseminated and networked, as appropriately and as rapidly as possible, to the law enforcement, intelligence, regulatory, and financial communities. Special attention is placed on providing feedback to the regulated industries through various publications and forums (FinCEN Advisories and Bulletins, SAR Review, Bank Secrecy Act Advisory Group Meetings) by highlighting the value of the information they are providing to law enforcement.

In fact, on September 13, 2001, just two days after the horrific attacks on our nation, FinCEN's expertise in money laundering and financial crime was quickly recognized and we were requested by law enforcement to provide immediate assistance to the investigation. The agency was well positioned to act quickly to this request because our programs already had been designed to provide exactly the type of comprehensive, interagency information analysis, sharing and support that is now needed in this nation's war against terrorism.

Law Enforcement Support

Law enforcement's need for value-added assistance on financial information is supported primarily through our Office of Investigations (OIV) and the Office of Strategic Analysis (OSA). OIV's programs are divided into two primary components: (1) Direct Case Support – consisting of an in-house staff of experts who respond to

requests for data searches and analysis by law enforcement; and, (2) Indirect Case Support – made up of two programs known as Platform and Gateway. In addition, FinCEN develops proactive targeting packages for law enforcement through OIV and the Office of Intelligence Liaison (OIL). OIL was established in late 1999 to proactively identify, through BSA data, clues or leads for law enforcement on possible terrorist-related finances and activities.

Direct Case Support

FinCEN's flagship program is its direct case support to approximately 300 law enforcement agencies. Through the use of advanced technology and numerous data sources, we link together various aspects of a case by adding value to what is already known by investigators. This ability to link to a variety of databases provides one of the largest repositories of information available to law enforcement in the country. Since 1990, we have provided support to more than 105,000 cases involving over 400,000 subjects to federal, state, local, and international law enforcement agencies.

Indirect Case Support

Both Platform and Gateway continue to be increasingly successful programs by permitting others to take advantage of our analytical and technological resources while using their own personnel. OSA adds further value to BSA data through trends and patterns analysis. This dual approach to maximizing the information contained in BSA data enables FinCEN to more efficiently meet the growing needs of our customers.

Identifying Financial Crime Trends and Patterns

The Office of Strategic Analysis provides analytical support to law enforcement and the intelligence community, through identification of trends, patterns and issues associated with money laundering and other financial crimes. BSA information, especially suspicious activity reports (SARs) filed by the nation's financial industries, is the foundation for developing our analytical products.

For instance, FinCEN just issued the 5th Suspicious Activity Report (SAR) Review -- Trends, Tips and Patterns in February 2003. This report specifically focuses on terrorist financing methods through Informal Value Transfer Systems (IVTS) such as hawalas, as well as through non-profit organizations. Also included in the report are several case summaries in which SARs and other BSA information played an important role in the success of an investigation and/or prosecution of criminal activity. (A copy of the report can be found on FinCEN's website at www.fincen.gov.)

The term IVTS is used to describe money or value transfer systems that operate informally to transfer money. In the past, some of those informal networks were labeled by various terms including "alternative remittance systems" and "underground banking." Depending on the ethnic group, IVTS can be referred to as "hawala" (Middle East,

Afghanistan & Pakistan); “hundi” (India); “fei ch ‘ien” (China); “phoe kuan” (Thailand); and “Black Market Peso Exchange” (South America).

For example, in some nations hawalas are illegal and in others they are active but unregulated. Therefore it is difficult to accurately measure the total volume of financial activity associated with the system. However, it is estimated that, at a minimum, tens of billions of dollars flow through hawalas and other informal value transfer systems on an annual basis. While the majority of IVTS activity is legitimate in purpose, some of these systems have been used to facilitate the financing of terrorism. The very features that make the systems attractive to legitimate customers – efficiency, convenience, trust, speed, anonymity, and lack of a paper trail – also make it appealing to terrorists and terrorist organizations.

Under the USA PATRIOT ACT, hawalas and informal value transfer systems are required to register as a money services business or MSB, thereby subjecting them to existing money laundering and terrorist financing regulations, including the requirement to file SARs. The Act also makes it a crime for the money transfer business owner to move funds that he knows are the proceeds of a crime or are intended to be used in unlawful activity. Failure to register with FinCEN and/or failure to obtain a state license also are federal crimes.

In the next few days, we will publish a FinCEN Advisory to further educate the financial community to potential vulnerabilities of IVTS in terrorist financing.

Strengthening International Cooperation

Recognizing the global nature of crime and the fact that the financial trail of U.S. law enforcement investigations often leads to other countries, FinCEN has been a key player in encouraging and working with other countries to develop effective anti-money laundering standards and mechanisms to further the exchange of information. In particular, FinCEN has been focusing on helping to promote the financial intelligence units (FIU) known as the Egmont Group. The international community’s response has been increasingly cooperative and membership in Egmont has grown from a handful of members in 1995 to the current membership of 69 countries.

Since September 11, 2001, the Egmont Group has taken steps to leverage its information collection and sharing capabilities to support our country in its global war on terrorism. Last October, FinCEN hosted a special Egmont Group meeting that focused on the FIUs’ role in the fight against terrorism. In conclusion, the FIUs agreed to: (1) work to eliminate impediments to information exchange; (2) make terrorist financing a form of suspicious activity to be reported by all financial sectors to their respective FIU; (3) undertake joint studies of particular money laundering vulnerabilities, especially when they may have some bearing on counter terrorism, such as hawala; and (4) create sanitized cases for training purposes.

Regulatory Area

In order to effectively administer the BSA, FinCEN relies on its regulatory partners – the five federal banking regulators (the Federal Reserve Board, the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the Office of Thrift Supervision, and the National Credit Union Administration), the Internal Revenue Service (IRS), the Securities and Exchange Commission, and the Commodities Futures Trading Commission. Each financial regulator administers its own anti-money laundering regulations and is responsible for the examination of those financial institutions within its respective jurisdictions regarding compliance with the BSA and the implementation of effective anti-money laundering programs. Non-compliant institutions may be referred to FinCEN for enforcement action in appropriate circumstances.

On March 6, 2003, FinCEN assessed a civil money penalty against Western Union Financial Services Inc. (“Western Union” or the “Company”) in the sum of \$3,000,000 for violations under the BSA. FinCEN determined that from January 1, 2002, through October 8, 2002, Western Union failed to file 662 SARs for structured transactions in violation of 31 U.S.C. §5318(g) and 31 CFR 103.20. The assessment includes a comprehensive undertaking by Western Union to ensure that its SAR monitoring system appropriately recognizes structured transactions, to file all SARs nationwide that should have been filed, and to maintain appropriate due diligence oversight with respect to its agents.

In January 2003, Banco Popular was charged with one count of failing to file Suspicious Activity Reports (SARs) in violation of Title 31 USC 5318(g)(1) and 5322(a). Banco Popular waived indictment, agreed to the filing of the information, and accepted and acknowledged responsibility for its behavior in a factual statement accompanying the information. The company will forfeit \$21.6 million to the United States to settle any and all civil claims held by the government. In light of the bank’s remedial actions to date and its willingness to acknowledge responsibility for its actions, the government will recommend to the court that any prosecution of the bank on the criminal charge be deferred for 12 months, and eventually dismissed with prejudice if the bank fully complies with its obligations. Concurrently, FinCEN has assessed a \$20 million civil money penalty for violations of the Bank Secrecy Act against Banco Popular for its conduct, which will be deemed satisfied by the payment of the \$21.6 million forfeiture.

These enforcement actions are posted on FinCEN’s website and serves to further notify and educate the financial community at large of BSA violations of a serious nature.

One of FinCEN’s primary responsibilities in administering the BSA is to conform its regulations to legislative mandates – mandates that reflect the changing realities of money laundering vulnerabilities within the financial community. For example, prior to the passage of the USA PATRIOT Act, we were in the process of expanding certain provisions of the BSA such as a broker/dealer SAR rule to financial sectors beyond the 21,000 depository institutions. Simultaneously, we were focusing on the implementation of a program for the money services business (MSB) industry, believed to number about

200,000 entities, as well as the casino industry. This effort was significantly accelerated by the passage of the USA PATRIOT Act. That universe now includes travel agencies, automobile and boat dealers, jewelry dealers, pawnbrokers, life insurance companies, mutual funds, operators of credit card systems, and certain segments of the securities and futures industries.

USA PATRIOT Act of 2001

This Committee recognized the need to expeditiously make additional tools available to law enforcement to fight money laundering and terrorist financing. It was the driving force behind the USA PATRIOT Act. This prompt action underscored the importance of pinpointing the nexus between crime and its associated financial activity in order to uncover valuable leads by building a financial trail. The Act's expansion of the scope of the BSA resulted in a dramatic increase in FinCEN's responsibilities, under BSA authorities. FinCEN was directed to implement 23 of the 44 provisions contained in Title III and also has a key role in many of the working groups established by Treasury to address many of the other provisions.

I would like to highlight the progress FinCEN has made to date on implementing many of these provisions. (See attached chart on accomplishments under the USA PATRIOT Act.)

Expanding the Requirements of Anti-Money Laundering Programs to more Financial Institutions

Section 352 requires all financial institutions, as defined by the BSA, to establish anti-money laundering programs, and authorizes FinCEN to issue regulations defining minimum standards for such programs, or alternatively, for institutions not already subject to BSA regulations, to exempt them. This is a potentially huge number of entities, many of which have never been subject to federal regulation aimed at their specific lines of business.

Our initial challenge was simply to define what these categories of entities included. There was almost no guidance in the legislative history of the BSA. FinCEN chose a risk-based approach – focusing first on traditional financial institutions, relying on existing regulatory programs already in place, and then expanding outward to the next group to try to first cover the most likely places a money launderer would go. Casinos were already subject to an anti-money laundering program rule issued by FinCEN. Banks were subject to anti-money laundering program rules issued by the five federal bank regulators. Building on this approach, we worked with the self-regulatory organizations (SROs) for broker-dealers and commodities futures merchants to craft a rule that the SROs could incorporate into their regular compliance examinations. The rules were in place and approved by the SEC and Commodities Futures Trading Commission by the USA PATRIOT Act deadline on date. In April 2002, we issued a rule that compliance by all these entities with the existing anti-money laundering program rules would be deemed compliance with Section 352.

At the same time, FinCEN and the Treasury Department targeted several industries for inclusion in the first wave of rulemaking – rules known as interim final rules, that would be effective without notice and comment, but which would provide an opportunity to those interested to submit comments. These were: money services businesses, mutual funds, and operators of credit card systems. It should be noted that there are no exemptions in the money services businesses rule.

Issuers and redeemers of stored value which had always been subject to CTR reporting, were now also included in other BSA regulations such as SAR reporting. With respect to the mutual fund rule, we are continuing our practice of partnering with federal functional regulations by delegating responsibility for compliance examinations to the SEC. The credit card operator rule applies to companies like Master Card and VISA that license others to issue their cards. It focuses on the areas of their business where the money laundering risk appears to be greatest – their authorization of foreign banks to issue their card. The rule imposes due diligence requirements on the operators, particularly with respect to countries that have poor anti-money laundering controls. These rules were all issued in April 2002. A decision was made to temporarily exempt the remaining financial institutions while a study is conducted on these industries.

In September 2002, FinCEN issued proposed rules mandating anti-money laundering compliance programs for life insurance companies and unregistered investment companies. The life insurance rule reflected our assessment that the money laundering risks in the insurance industry were concentrated in the products offered by life insurers, including annuities. The unregistered investment company rule encompasses what are commonly known as hedge funds, private equity funds, commodity pools, and real estate investment trusts. The comment period on these rules has closed and they are being finalized. In February 2003, we published a proposed rule that would require dealers in precious metals, stones and jewels to implement anti-money laundering programs, and also published two advance notice of proposed rulemaking seeking comment on whether anti-money laundering program requirements should be extended to vehicle sellers and travel agents.

SAR Rules

Expansion of SAR requirements to industries where such reporting can be a valuable aid to law enforcement has been a priority, whether or not specifically required by the USA PATRIOT Act. On July 1, 2002, FinCEN issued a final SAR rule requiring broker-dealers to report suspicious transactions involving at least \$5,000 (the same threshold as for banks). On September 26, 2002, FinCEN issued a final rule requiring casinos to report suspicious transactions at the same threshold. Although the casino rule was not mandated by the Act, we believed the industry was important to cover. In October 2002, FinCEN published a proposed rule that would require life insurance companies to file SARs, also at the \$5,000 threshold. The comment period has closed on that rule and it is in the process of being finalized.

At the same time, FinCEN published a proposed rule that would include currency exchangers in the MSB SAR rule, which issued in final form on February 10. Most recently, last month, FinCEN issued a proposed rule that would require mutual funds to file SARs. The comment period for that rule closes on March 24, 2003. Pursuant to the Act's mandate, FinCEN is consulting with the CFTC about extending SAR requirements to commodities professionals. It is important to note that these rules have been developed in consultation with law enforcement and the relevant regulators, and with full consideration of comments by the affected industries.

Cooperative Efforts to Deter Money Laundering

One of the most challenging tasks given to FinCEN has been to develop new ways to share information between law information and financial institutions, and to enable financial institutions to share information among themselves. Initially, working with law enforcement, we identified a gap in our quick response capability – we had no way to have an immediate search done throughout the financial sector to locate funds associated with a terrorist financing or money laundering scheme.

FinCEN, therefore, developed a system – a combination of e-mail and blast fax – that could quickly transmit names of suspects to financial institutions and get back reports of matches within days. The system was not designed to get documents or substitute for subpoenas – but rather to serve as a locator that could be followed up with subpoenas or other appropriate legal process. The regulations requiring financial institutions to respond to such queries – where the government had credible evidence of money laundering or terrorist financing -- became final in late September 2002. The system became operational in November 2002 and FinCEN received valuable information from financial institutions on cases involving both terrorist financing and money laundering.

Although these responses were helpful, there were still technical changes that needed to be made. So, after consulting with law enforcement and regulators, FinCEN placed a temporary moratorium on further Section 314 requests so that it could streamline the process, make it more manageable and less burdensome, and through the federal regulators, better educate the community about what was being expected of them.

The moratorium was recently lifted and we are hopeful that the improvements made to the system will provide critical, time-sensitive information to law enforcement, without unnecessary complexity and burden. This is very much a work in progress and we will continue to tweak the system to make it better. Also, I would like to add that FinCEN is greatly indebted to the substantial assistance that it has received from the regulators and the law enforcement community.

I also want to note that Section 314(b) required us to promulgate regulations permitting financial institutions to share information among themselves regarding individuals and entities suspected of engaging in terrorist financing or money laundering. Our regulation extends to all financial institutions that are required to have anti-money

laundering programs. Such institutions, may, upon filing a notice with FinCEN, share such information with other similarly qualified financial institutions for the purpose of identifying and reporting on such activity, complying with the BSA, and determining whether to engage in a transaction. The information cannot be used for any other purpose, and its security and confidentiality must be safeguarded.

Electronic Filing of BSA Reports

Closely related to Section 314 is Section 362 requiring FinCEN to develop a highly secure network to allow financial institutions to file BSA reports electronically and to supply financial institutions with alerts and other information regarding suspicious activities that warrant immediate and enhanced scrutiny. I am pleased to inform you that we moved very swiftly to develop the PATRIOT Act Communications System or PACS. A 60-day pilot program that included the voluntary participation of approximately 30 institutions was successfully concluded and on October 1, 2002, PACS became fully operational.

Financial institutions are not mandated to use PACS, but the system does provide a third, cost-effective option for filing CTRs and SARs. PACS allows participating financial institutions to electronically file CTRs and SARs in a highly secure fashion via the Internet, including both single forms and electronic batches of forms. PACS accelerates the delivery of BSA information to federal and state law enforcement and it reduces the expense to the financial institution by eliminating the need for magnetic tapes and paper forms.

Verification of Identification

Section 326 of the USA PATRIOT Act requires financial institutions to verify customer identification in connection with the opening of accounts. The Treasury Department is required to delineate the required procedures in rules jointly issued with the federal banking, securities, and commodities regulators. In July 2002, FinCEN issued a series of proposed rules jointly with the five federal bank regulators, the SEC, and the CFTC, that would delineate customer identification programs (CIPs) for entities regulated by these agencies, as well as a proposed rule issued solely that would delineate CIPs for non-federally regulated banks that are subject to the BSA. The proposals were the subject of substantial comment. Crafting final rules that are clear and consistent across these industries that can be jointly issued with seven other agencies as required by Section 326 has been a great challenge. We are working hard with these seven agencies and the Department of Treasury to complete this task.

Special Measures for Jurisdictions, Financial Institutions, or International Transactions of Primary Money Laundering Concerns

Section 311 authorizes the Secretary of the Treasury to impose special measures against jurisdictions, financial institutions, or one or more classes of transactions that are found to be of primary money laundering concern. The measures that may be imposed,

after consultation with the State and Justice Departments, and the federal functional regulators, range from increased recordkeeping requirements to an absolute prohibition on the maintenance of correspondent accounts in the United States for the designee. After engaging in the required consultations, in December 2002, Treasury designated Ukraine and Nauru as jurisdictions of primary money laundering concern.

Special Due Diligence for Correspondent Accounts and Private Banking Accounts

Section 312 requires financial institutions that maintain correspondent accounts for foreign financial institutions to implement due diligence procedures, and in certain cases enhanced due diligence procedures, concerning their correspondents. It also requires due diligence procedures for private banking accounts, and enhanced due diligence procedures for private banking accounts of senior foreign political figures to detect and report transactions involving the proceeds of foreign corruption. In May 2002, we issued a proposed rule under Section 312, and in July 2002 we issued an interim final rule applying the correspondent account requirements to banks, and the private banking account requirements to banks, broker-dealers and futures commission merchants. We are completing work on a more detailed and comprehensive final rule.

Reporting of Suspicious Activities by Underground Banking Systems

FinCEN has worked diligently over the past year examining the workings of the Informal Value Transfer Systems (IVTS), such as hawalas, and has issued a report to the Congress, as required under Section 359 of the USA PATRIOT Act on suspicious activities of such systems. Fieldwork and analysis of the data gathered presented the following findings: (1) existing BSA regulations are applicable to the U.S.-based operators of IVTS; (2) current research does not suggest an immediate need for additional legislation; (3) existing BSA rules should be reexamined to enhance regulatory compliance among operators of IVTS; and (4) the law enforcement and regulatory communities should undertake a comprehensive program to enhance their knowledge concerning the range of mechanisms used in IVTS.

Law Enforcement Access to Currency Reports by Non-Financial Businesses (Form 8300)

Section 365 of the Act required that the Treasury Department prescribe new regulations for filing currency reports by non-financial businesses with FinCEN. (Before the Patriot Act became law, the Internal Revenue Service (IRS) was required to collect Form 8300 information under Section 6050I of the Internal Revenue Code. This information was considered tax return information and was not readily available to law enforcement.) FinCEN worked diligently with Treasury to issue these new regulations and on December 20, 2001, an interim rule and a companion notice of proposed rulemaking were issued. As of February 20, 2002, FinCEN began receiving downloads of the 8300 data from IRS several times a week. FinCEN analysts use this information in the same manner as other BSA information in order to add value to law enforcement investigations.

Conclusion

Madam Chairwoman, in closing, the threats we deal with today have taken on new dimensions from those that existed when the legal structure for anti-money laundering was first created. Traditional methods for laundering have mutated over time to take advantage of new technologies, diverse institutions and industries. The financial channels of terrorism have traversed all of these changes, creating an urgency for seeking greater cooperation among governments, law enforcement, regulators, and the regulated industries to share and disseminate information as never before. It is an undertaking to which all of the employees at FinCEN are deeply committed, while preserving our core values, including our accountability for what we do with the masses of data entrusted to us.

On behalf of FinCEN, I would like to thank you for this opportunity to discuss with you our accomplishments as well as our unique role in the fight against terrorist financing. I would be happy to answer any questions you may have at this time.